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SUBJECT: ISTANBUL BUSINESS LEADERS FOCUS ON EU

REF: ANKARA 5791

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1. (SBU) Summary: In separate meetings the week of November 8, Istanbul business leaders told visiting State Department Special Representative for Commercial and Business Affairs Frank Mermoud and U.S. Ambassador to the European Union Rockwell Schnabel that they are optimistic both about Turkey's overall economic prospects and about the outcome of the December 17 EU summit. Business leaders were relatively pragmatic about the October 6 EU Commission report, recognizing the balance it sought strike between Turkey and sceptical European publics. They stressed, however, that there should be no dilution of the ultimate goal of full Turkish membership in the EU. Only that prospect, they argued, will make Turkey's reform process irrevocable and overcome the entrenched interests that will otherwise resist surrendering the concessions and privileges they now enjoy. A cautionary note was struck by TUSIAD foreign relations chief Cem Duna, who warned that the negotiations will highlight the divergent interests of different parts of the Turkish economy, and that it will not be easy for the country to formulate a common negotiating position. End Summary.

2. (U) The November 8 visit of Special Representative Mermoud and November 10-13 visit of USEU Ambassador Schnabel permitted us to touch base with a broad cross-section of the Istanbul business community and regauge sentiment both about Turkey's current economic conjuncture and about prospects for Turkey to receive a date to begin negotiations at the EU's December 17th summit. Mermoud's meetings ranged from bilateral business groups such as the American Business Forum in Turkey and the Turkish-American Business Association, to the Foreign Investors' Association (YASED) and such leading American investors as Coca-Cola, Cargill and Motorola. In addition to TUSIAD (the Turkish Businessmen's and Industrialist's Association), Ambassador Schnabel also met with representatives of the Turkey-EU Business Council, ING Bank Managing Director John McCarthy and Finansbank Chairman Husnu Ozyegin.

3. (U) Bullish Outlook: Both Mermoud and Schnabel's interlocutors were generally upbeat on Turkey's prospects in the near to mid-term. ING's McCarthy noted that Turkey is currently experiencing the best economic period he has seen in his twenty-plus years in Turkey. He stressed that the bank, while "realistic" about problems that continue to exist, such as corruption and an inadequate legal system, is generally "bullish" on Turkey. Cem Duna, TUSIAD's foreign relations chief (and a former Turkish Ambassador to the EU), echoed this positive appraisal, pointing not just to the work that has been done in recent years to restore "macro balances" in the economy, but also structural changes such as the creation of independent regulatory boards that are now working "more or less" effectively. He noted that work has also begun on legal reform, though he conceded that with only 10,000 judges and prosecutors for a population of 70 million people, Turkey still has a long way to go. EU Business Council leaders pointed up their expectation that the ongoing economic recovery will enable the country to overcome some of the limitations that have held it back in the past. Turkey's underdeveloped capital markets, for instance, have suffered from the absence of institutional investors, but with the recent creation of private pension plans and the prospect of development of a mortgage system in the next two years, there is hope that these markets can be deepened and strengthened. Only Cargill's Corporate Affairs Director Mustafa Sayinatac was more pessimistic about Turkey's mid-term prospects, pointing to such issues as Turkey's budget and current account deficits, the absence of foreign direct investment, and his belief the economy is overheating. McCarthy, however, opined that this year's growth and current account deficit reflect the satisfaction of pent-up demand and will ease next year: ING sees growth moderating to 4.8 percent in 2005, he said.

4. (SBU) An EU Stamp of Approval: Business leaders stressed their belief that Turks feel a strong emotional pull to

Europe, based in large part on the belief that EU membership will bring about an improvement in the standard of living here. For business, Duna said, the key advantage the EU will bring is "predictability." Business council leaders elaborated that they expect that some of the key problems which currently hamper their activities, such as red tape and an inadequate legal system, will be addressed as part of the negotiating process. While (like Duna) they were generally understanding of the balance the commission had sought to strike in its October 6 report, they stressed the importance of avoiding "additional qualifiers" on December 17, since this would reduce the impact of a positive decision. The key, they suggested, is that the "carrot of full membership" remain clearly in front of Turkey, since only that prospect will convince economic actors here to be willing to give up the concessions and privileges that they have enjoyed in the past. Not all saw the report's emphasis of the "open-ended" nature of the negotiations as all negative, however. Tezcan Yaramanci, Chairman of BankEuropa, reflecting a viewpoint we are hearing more and more from the business community, noted that this may work to Turkey's benefit, since once it has made the changes necessary to join Europe (and benefited economically from them), it may find that it no longer wants to join the club.

15. (SBU) Challenges Ahead: All agreed that the challenges facing Turkey will only intensify after December 17. Duna, who is often mentioned as a candidate for the post of Secretary General of Turkey's EU negotiating team, noted that

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he is concerned about the difficulties that the negotiating process will pose for Turkey as it attempts to formulate national positions on various economic issues. "The fault lines will be more obvious," he predicted, and companies will be divided based on the nature of their operations. Cargill's Sayinatac pointed to the difficulties that will result from the need to reconcile Turkey's enormous agricultural sector with that of the EU, while Coca-Cola's Bozer dismissed the argument that large Turkish companies are not ready for the EU ("the Customs Union has prepared them"), but conceded that he is concerned about how Turkish SMEs will react. Most, including members of Turkey's EU business councils, concurred that there is currently little understanding in Turkey, even among specialists, about what EU membership actually entails and about the changes that Turkey will be asked to undertake. They predicted more than a few difficult moments as Turkey is asked to make changes to harmonize with the acquis.

16. (SBU) Foreign Investment: All agreed that while the EU stamp of approval, a sort of ISO 9000 certificate, will mark a "paradigm shift" for both the EU and Turkey, by itself it will not be enough to spark an inflow of foreign direct investment. Business council leaders pointed to ongoing problems such as red tape, heavy taxation, and Turkey's legal system as factors that will take time to address, so that even with a date Turkey will remain "far down the list" of potential investment locations. Coca-Cola President Ahmet Bozer, whose own company's IPO was pulled on the day he met with Mermoud, predicted that investment would flow only after the "tipping point" in negotiations is reached and Turkish EU membership appears inevitable. Mustafa Alper, YASED's new Secretary General, noted that his organization is seeing

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increased interest in Turkey, particularly from Asian countries, as it draws nearer to the EU. But he conceded that this has not yet translated into new flows of FDI and that while much new legislation has been adopted, implementation issues remain. The "bureaucracy is tough," he noted, and it will take time to tackle it, legal reform, and taxation. He added that while the government has been extremely responsive on many issues, outstanding areas of dispute do remain. Most notably, private sector/government disagreement over how a new Investment Promotion Agency should be structured and managed has resulted in its being put on hold for the foreseeable future. Overall, however, he assessed that the investment climate remains "cloudy, but is getting better."

17. (SBU) Comment: Ambassador Schnable and Special Representative Mermoud's meetings provided a useful snapshot of where Turkish business is in its thinking about the Turkish economy generally and EU relations specifically. Optimism was widespread that Turkey will receive a date on December 17, that will enable it to take its relationship with the EU, and its economy as well, to a new level. Few were eager to speculate about an alternative "doomsday" scenario, though most agreed that failure to secure a date would result in a sharp economic correction and threaten the country's hard won political and economic stability. Duna predicted that such a development would lead opposition forces (whether in the establishment or fundamentalist circles) to challenge the reforms that Turkey has achieved in recent years. But he expressed hope that those changes have

already become so entrenched that the Turkish people would not accept going back to the old way of doing things even even in such a worst case scenario. End Comment.
SMITH